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‘So Catastrophic': How a Debt Ceiling Breach Would Hurt Schools

By Mark Lieberman — May 17, 2023 8 min read

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If Congress doesn’t raise the federal government’s debt ceiling, America will default on its debt obligations in a matter of weeks, potentially triggering a worldwide economic crisis that would almost immediately pose major and lasting trouble for K-12 schools.

Education advocates on Capitol Hill are fretting over the consequences of a default that could happen as early as June 1. Such a default has never happened before, leaving most wondering how exactly it would play out.

If a default happens before July 1, the federal government might be unable to distribute billions of dollars for high-need students, special education services, and English-language instruction. Because school districts—many of which have already set their budgets for the coming year—count on those funds, teacher layoffs, academic program cuts, and administrative chaos could ensue.

Longer term, the economic turmoil that could result from a default, including a possible recession, would lead to fewer resources and greater fiscal challenges for schools—diminished state tax revenue for education, difficulty borrowing money for construction projects, and depressed returns on pension funds for school employees.

“The results will be so catastrophic,” said Sarah Abernathy, executive director of the Committee for Education Funding, a nonprofit that advocates for federal investments in education. “There’s a ton of uncertainty, and none of the outcomes are good.”

Many district leaders have been so busy with the end of the school year and ongoing school funding debates in state legislatures that the debt ceiling fight is only beginning to emerge on their radar, said Kevin Brown, executive director of the Texas Association of School Administrators.

“To some degree people have become numb to the divisiveness at the federal level,” Brown said. “But if [default] happens, I think people will have a renewed sense of urgency and be pushing pretty hard to get those funds.”

Why is this happening?

Congress has the power to raise the limit on the amount of debt the country can accrue at one time. Currently that limit is $31.4 trillion. U.S. Secretary of the Treasury Janet Yellen said recently that the “X-date,” when the federal government needs to borrow more money to pay its bills, could arrive as early as June 1.

Failure to raise the debt ceiling could cost the country 8 million jobs and trigger a recession on the scale of the one in 2008, according to an analysis by Moody’s .

President Joe Biden and top officials in Congress have been debating for weeks over how best to avoid the crisis. The House of Representatives, led by a slim Republican majority, wants to couple the debt limit increase with cutting from the federal budget billions of dollars for nondefense programs, including K-12 education. Biden and Democrats in Congress have pushed for a "clean" debt limit increase with no other changes.

The debt limit has come up for debate numerous times in recent years. In 2011, a divided Congress reached an agreement with then-President Barack Obama to cap federal spending through a process called "sequestration" in exchange for raising the debt ceiling. Federal education spending took a major hit as a result of sequestration, hitting schools with large swaths of federal land within their district boundaries particularly hard.

More recently, during the administration of President Donald Trump, Republicans approved clean increases to the debt limit while they maintained control over the presidency and both chambers of Congress.

Meanwhile, Biden's advisers have been considering a range of other possibilities for addressing the debt limit without help from Congress, including invoking the 14th Amendment to assert that the debt limit itself is unconstitutional. But Biden has said he's worried that assertion would be challenged in court.

Why does timing matter?

Most federal funding programs for K-12 schools are forward-funded , which means schools receive funds during the last quarter of the federal fiscal year that they can use for the following fiscal year. The federal fiscal year runs from Oct. 1 through Sept. 30, with the last quarter beginning July 1.

If default happens before then, the federal government could be out of money to send states their allocations under Title I (which serves high-need students), Title III (English learners), the Individuals with Disabilities Education Act (special education), and other programs. Most districts have already set their budgets for the upcoming school year with the assumption they'll be getting that money. They might be forced to lay off employees and cut programming if they don't receive it.

The timing of the resolution to the default crisis is key, however.

If the country's top officials can achieve a "cure" relatively quickly after a default, the delays to education funding might be minimal. But a longer process could mean that laid-off employees find other work and aren't willing to come back when the funding for their positions finally becomes available, Abernathy said.

Some ongoing competitive grants might also be paused if a default constrains the federal government's spending power, Abernathy said. Programs that could be affected include funding opportunities for literacy instruction, school safety and mental health investments, and charter schools looking to open or expand.

Summer school programs that offer breakfast and lunch may also be in trouble if federal funding for school meals dries up, Brown said.

In general, superintendents prefer that funding streams be predictable, and that they know what they can expect well in advance. Otherwise, they instinctively avoid planning big investments for fear of not getting the funds they're owed, Brown said.

"If [the disruption caused by the default lasted] just a day or two or a week, I think schools would probably come out OK," Brown said. "At some point it will be a problem for school districts in their cash flow, as well as in their programming."

How much school funding would be affected by a default?

The federal government supplies roughly 8 to 10 percent of the country's overall spending on public schools.

But much of that aid is designed to help school districts offer equitable access for students who need additional resources—poor students, students with disabilities, English learners. Losing access to it, even for a short time, could have outsized negative effects.

"A lot of what they're doing is equity-based—helping out states that don't have as many resources to provide public education or aren't taxing themselves as much," said Robert Wassmer, a professor of public policy and administration at California State University, Sacramento who has written about the intersection of K-12 schools and the economy . "We view education as a national good."

If the federal government can't fulfill its commitments to schools because of a default, states may face pressure to step in, Wassmer said, especially if they still have surplus revenue on hand from the surge in tax collections that followed the pandemic.

Schools are already bracing for cuts as the surge of federal COVID relief funds they got in 2020 and 2021 begin to run out. Now they're contending with the prospect of "cuts on top of cuts," said Trisha Schock, executive director of administrative services for the North Central Educational Service District, which serves several school districts in and around Wenatchee, Wash.

Pension obligations could also strain districts' budgets more severely than they already do if the federal government shuts down upon a debt ceiling breach, said Anthony Randazzo, executive director of the Equable Institute, a bipartisan nationwide nonprofit that conducts research and advocacy on improving pension systems.

Because pension spending in many states is tied to school district payroll, districts would continue to need to pay their share of the cost of teacher pensions regardless of any decline in federal spending.

Pension funds could also see depressed returns on their investments if the stock market tumbles—one of the surest, short-term consequences of a default. If that dip in the market is sustained, states and school districts would be on the hook to pay out obligations that pension funds can no longer cover with their investments.

On the other hand, if the cost of borrowing increases as a result of the default, pension funds might have more opportunities to buy federal bonds, essentially lending money to the federal government and increasing their returns in the process.

That upside wouldn't erase the substantial impacts of an economic downturn, though.

"My bet would be that any benefits from increased bond yield would be outweighed by the net negatives of federal default," Randazzo said.

What should school leaders do?

Take stock of your overall fund balance and federal share. Which programs are fueled purely by federal dollars? Can other money be shifted over to cover those expenses if federal funds go away? Wassmer thinks districts need to become extra savvy about where their money is coming from and how much wiggle room they have.

Contact your state education department. Elleka Yost, director of advocacy for the nationwide Association of School Business Officials, recommends school district officials ask state leaders if they've received any communication from the federal government about what might happen, or if there are any plans in place to mitigate disruption.

Expect the unexpected. America has never defaulted on its debt obligations before, and all predictions about what might happen next are based on informed speculation.

"My guess is people haven't done a ton of thinking about it because it's so uncertain," Abernathy said. "You have 18 contingency plans and you need a 19th one."

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